

IN THE UNITED STATES BANKRUPTCY COURT FOR THE
WESTERN DISTRICT OF MISSOURI

IN RE:)	
)	
GAELA A. HEDRICK,)	Case No. 00-40244
)	
Debtor.)	
)	
EASTERN STATES LIFE INSURANCE)	Adversary No. 00-4151
COMPANY,)	
)	
Plaintiff,)	
)	
v.)	
)	
BRUCE STRAUSS,)	
Chapter 7 Trustee, and)	
GAELA A. HEDRICK,)	
)	
Defendants.)	

MEMORANDUM OPINION

Eastern States Life Insurance Company (Eastern States) filed this adversary proceeding and a motion for summary judgment in order to recover its alleged property from this Chapter 7 bankruptcy estate. This is a core proceeding under 28 U.S.C. § 157(b)(2)(K) over which the Court has jurisdiction pursuant to 28 U.S.C. § 1334(b), 157(a), and 157(b)(1). The following constitutes my Findings of Fact and Conclusions of Law in accordance with Rule 52 of the Federal Rules of Civil Procedure as made applicable to this proceeding by Rule 7052 of the Federal Rules of Bankruptcy Procedure. For the reasons set forth below, I find that Eastern States does not hold a properly perfected security interest, therefore, I will deny its motion for summary judgment, enter judgment in favor of

the Chapter 7 trustee and debtor Gaela A. Hedrick, and allow Eastern States' claim as a general unsecured claim.

FACTUAL BACKGROUND

On May 25, 1995, debtor Gaela Hedrick settled a personal injury lawsuit. Pursuant to a Release and Settlement Agreement, the tort defendants made an assignment to Metropolitan Life Insurance and Annuity Company (Metropolitan) to pay Hedrick the sum of \$3,413.00 per month for a term of 30 years, commencing on July 1, 1995, and increasing by 3 percent every July 1, thereafter.

On December 29, 1997, Hedrick, whose address was 499 Dixie Heights Road, Kirbyville, Taney County, Missouri 65679 on that date, voluntarily entered into an agreement with Colonial Financial Services, Inc. (Colonial), whereby, in exchange for a lump sum payment of \$128,000, Hedrick unconditionally and irrevocably assigned to Colonial her right to receive a portion of the Metropolitan payment (the Colonial Agreement).¹Pursuant to the terms of the Colonial Agreement, Metropolitan would pay to Colonial \$2,000.00 per month commencing on February 1, 1998, and ending on January 1, 2008. The payment of \$2,000.00 would increase by 3 percent on July 1, 1998, and on every July 1 thereafter, until January 1, 2008. On January 19, 1998, Colonial assigned its rights to Eastern States. On January 30, 1998, Colonial filed a UCC-1 Financing Statement with

¹Pl. Ex. # 6.

the Secretary of State for the State of Missouri.² The Financing Statement covers the following:

All debtor's right, title, and interest in and to the following described annuity policy and release obligations under that certain Purchase and Sale Agreement dated December 29, 1997, between debtor and secured parties shown herein. Annuity Policy # 50076 issued by Metropolitan Life Insurance Company on July 1, 1995. General Release for Internal Structured Settlement dated and between the parties as set forth herein.³

On February 20, 1998, Colonial filed a "Statements of Continuation, Partial Release, Assignment, Etc. – Form UCC-3" with the Secretary of State for the State of Missouri giving notice of the assignment to Eastern States.⁴

Hedrick testified that commencing February 1, 1998, Metropolitan sent a monthly check made out to the Gaela Hedrick Irrevocable Trust to Colonial. Colonial then stamped Gaela Hedrick's name, cashed the check, kept its payment, and sent the balance to Hedrick. This pattern continued until September of 1999.

On April 5, 1999, Hedrick filed a Chapter 11 bankruptcy petition in California. The California Court converted the case to Chapter 7 on July 20, 1999, and subsequently transferred the case to this Court for the convenience of the parties. On August 2, 1999, this Court entered an Order converting the case to Chapter 7. Bruce E. Strauss is the Chapter 7 trustee (the Trustee). In September of 1999 Metropolitan ceased sending payments to

²Pl. Ex. # 9.

³Id.

⁴Pl. Ex. # 2.

Colonial, care of the Gaela Hedrick Irrevocable Trust, and began sending them, instead, to the Trustee. The Trustee objected to Hedrick's attempt to exempt annuity payments. The Trustee and Hedrick then agreed that the objection to the exemption would be sustained, and that the Trustee would receive 25 percent of the monthly annuity payments with Hedrick to receive 75 percent.⁵

Eastern States made a demand upon the Trustee for its alleged portion of the annuity payment. Eastern States claims that it purchased a portion of the annuity payments from October of 1999 through January of 2008. It further claims that such portion of the payment is, therefore, not property of the bankruptcy estate and should be turned over. The Trustee offers two affirmative defenses. He first claims that Hedrick's agreement with Colonial, hence Eastern States, is without force and effect because the structured settlement contains a non-assignment clause. He next claims that Eastern States' security interest is not properly perfected. On June 4, 2001, Eastern States filed a motion for summary judgment. On June 18, 2001, this Court held a hearing on both the Complaint and Eastern States' motion for summary judgment. At the hearing both Hedrick and Paul Nichols, a vice-president of Eastern States, testified. As announced at the hearing, I will deny Eastern States' motion for summary judgment. And, since I find that the perfection issue is dispositive of this matter, I will not reach the issue of the effect of a non-assignment clause in a structured settlement.

DISCUSSION

⁵Case No. 00-40244, Doc. # 89 (Order Sustaining Trustee's Objection to Exemptions).

The structured settlement is a contract, and Hedrick's right to receive annuity payments from Metropolitan for a term of 30 years arises from that contract. As such, it is a contract right. There was some discussion at the hearing regarding whether the transaction between Hedrick and Colonial was a loan or sale. The transaction is documented in the Purchase and Sale Agreement as a sale.⁶ Hedrick testified, however, that she approached Colonial to borrow money. She stated she needed the money to consolidate all of her debts, pay them off, and pay her attorney's fees. She said she advised Colonial that the annuity was not assignable, and that Colonial assured her that she could redirect the payments, even if she could not assign the annuity itself. She testified that she thought of the transaction as a loan, even though there is language in the document that states otherwise. Paragraph 3.14 of the Purchase and Sale Agreement states in bold letters, "**This is Not a Loan.**" Hedrick, nonetheless, stated that she intended to repay the loan at the time she incurred it. For purposes of this dispute, I find it irrelevant whether this was a sale or a loan because Hedrick intended to grant Colonial a security interest in the stream of payments either way. Security interests are interests in personal property that secure payment of an obligation.⁷ And a buyer may acquire a security interest by complying with the requirements of Article 9 of the Uniform Commercial Code (the UCC). Article 9 sets out a comprehensive scheme for the

⁶Pl. Ex. # 6.

⁷Mo. Stat. Ann. § 400.1-201(37) (1994); Doss v. Syntex Agribusiness, Inc., 901 S.W.2d 293, 297 (Mo. Ct. App. 1995).

regulation of security interests in personal property.⁸ While the UCC no longer defines contract rights as a separate category of personal property, it includes them as a general intangible.⁹ And, I note, that Colonial, as the buyer, treated the Purchase and Sale Agreement as a secured transaction by filing a UCC-1 Financing Statement. I, therefore, find that Colonial “bought” from Hedrick her right to receive a portion of the Metropolitan annuity for a period of 10 years in exchange for \$128,000.¹⁰ Hedrick granted Colonial a security interest in this right, and Colonial attempted to perfect its security interest by filing a UCC-1 Financing Statement with the Missouri Secretary of State.

In Missouri, a secured party perfects a security interest in general intangibles by filing a financing statement in the proper place.¹¹ Perfection is necessary to preserve the priority of the lien, since the UCC provides that an unperfected security interest is subordinate to the rights of a person who becomes a lien creditor before the security interest is perfected:

(1) Except as otherwise provided in subsection (2), an unperfected security interest is subordinate to the rights of

. . .

⁸Mo. Stat. Ann. § 400.9-101, UCC Comment (1994).

⁹See Mo. Stat. Ann. § 400.9-106, UCC Comment (1994) (stating that the “term ‘general intangible’ brings under this Article miscellaneous types of contractual rights and other personal property which are used or may become customarily used as commercial security”). See also Pacific American Real Estate Fund, Ltd. v. Kansas City Power & Light Co., 633 S.W.2d 285, 288 (Mo. Ct. App. 1982) (stating that it is not necessary to determine if certain forms of collateral are contract rights, because if not, they are general intangibles).

¹⁰See Pl. Ex. # 6.

¹¹Mo. Stat. Ann. §§ 400.9-302(1) and 9-401(1)(c) (1994).

(b) a person who becomes a lien creditor before the security interest is perfected.¹²

The Bankruptcy Code (the Code) grants the bankruptcy trustee, as of the commencement of the case, the rights and powers of a hypothetical judicial lien creditor:

(A) The trustee shall have, as of the commencement of the case, and without regard to any knowledge of the trustee or of any creditor, the rights and powers of, or may avoid any transfer of property of the debtor or any obligation incurred by the debtor that is voidable by—

(1) a creditor that extends credit to the debtor at the time of the commencement of the case, and that obtains, at such time and with respect to such credit, a judicial lien on all property on which a creditor on a simple contract could have obtained such a judicial lien, whether or not such a creditor exists.¹³

Thus, the trustee is deemed to have a lien on all lienable property of the debtor. The hypothetical lien is inferior to any existing perfected lien at the time the petition is filed, and the hypothetical lien is superior to any unperfected lien. Moreover, section 544 of the Code relieves the Trustee from the effect of section 400.9-401((2) of Missouri's Revised Statutes.¹⁴ Section 400.9-401(2) provides a good faith exception to a secured creditor who files in the wrong place, or not in all of the proper places, against any person who had knowledge of the improperly filed financing statement.¹⁵ In other words, knowledge is not a

¹²Mo. Stat. Ann. § 400.9-301(1)(b) (1994) and UCC Comment, Purposes, ¶ 1.

¹³11 U.S.C. § 544(a)(1).

¹⁴See Gordon Square Pharmacy, Inc. v. Harris Wholesale Co. (In re Gordon Square Pharmacy, Inc.), 138 B.R. 533, 535 (Bankr. N.D. Ohio 1992).

¹⁵Mo. Stat. Ann. § 400.9-401.1(2) (1994).

defense to an improperly filed financing statement by dint of section 544 of the Code.¹⁶

In Missouri, the proper places to perfect a security interest in general intangibles are both in the office of the Secretary of State and in the office of the recorder of deeds of the county where the debtor resides:

(1) The proper place to file in order to perfect a security interest is as follows:

. . .

In all other cases, in the office of the secretary of state and in addition, if the debtor has a place of business in only one county of this state, also in the office of the recorder of deeds of such county, or, if the debtor has no place of business in this state, but resides in this state, also in the office of the recorder of deeds in the county in which he resides.¹⁷

It is undisputed that Hedrick resided in Taney County, Missouri on December 29, 1997, when she entered into the Purchase and Sale Agreement with Colonial. And the record indicates that she lived in that county until sometime in January of 1999, when she moved to California. The parties stipulate that there is no UCC-1 Financing Statement on file in Taney County, Missouri.¹⁸ Thus, I find that neither Colonial nor Eastern States ever properly perfected its security interest in a portion of the annuity payments by filing a UCC-1

¹⁶Gordon Square Pharmace, 138 B.R. at 535.

¹⁷Mo. Stat. Ann. § 400.9-401(1)(c) (1994); State of Missouri v. Kerr, 509 S.W.2d 61, 62 (Mo. 1974); In re Cox, 241 B.R. 651, 654 (Bankr. W.D. Mo. 1999); Budd Leasing Corp., v. Mid-Missouri Energy Corp. (In re Mid-Missouri Energy Corporation), 34 B.R. 58, 60 (Bankr. W.D. Mo. 1983).

¹⁸Doc. # 35.

Financing Statement in both the office of the Secretary of State and in the office of the recorder of deeds for Taney County, Missouri. Whether Colonial purchased a portion of the annuity payments, or whether Hedrick borrowed money and used the payments as collateral for the loan, does not change the outcome. Eastern States held an unperfected security interest on the date Hedrick filed her bankruptcy petition, therefore, Eastern States' claim is subordinate to the claim of the Trustee. The Metropolitan annuity payments are property of this bankruptcy estate, and Eastern States holds a general unsecured claim against that estate.

In accordance with this Memorandum Opinion, I will enter an Order denying Eastern States motion for summary judgment and a judgment in favor of the Trustee as to this adversary proceeding.

/s/ Arthur B. Federman
Chief Bankruptcy Judge

Date: July 26, 2001

Copy of the foregoing mailed electronically or conventionally to:

Bruce E. Strauss
James T. Lorenzetti
James H. Arneson

